47. The gestation period of new cable projects (including projects already on the drawing board or under construction) is in the range of only 2-3 years.[18] Hence, any hoped-for monopoly rents available from charging supra-competitive prices for submarine cable capacity are likely to be short-lived and are unlikely to offset the loss of volume that would swiftly follow.

48. Capacity expansion on existing submarine cables has even lower barriers impeding its entry into the market. The throughput capacity of existing cables can be expanded by upgrading the electronics at each end. The incremental unit cost of expanded capacity (i.e., the total incremental cost of the upgrade divided by the total number of new circuits yielded by the upgrade) is only about 1/4 to 1/3 the unit cost of the totality of capacity on a new line. *Id.* at 8. As with new capacity, the risk of stranding sunk costs of expansion can be minimized by obtaining capital commitments from the owner-participants and long-term volume commitments from carriers that merely wish to lease capacity. *Id.* at 12-13.

49. The number and size of recent and forthcoming new cable projects and expansion projects underscore the absence of significant entry barriers. *See FCC Circuit Status Report*, Table 7. Significantly, many of these projects were and are undertaken by Global Crossing and other non-consortium operators.

50. The absence of significant entry barriers means that submarine cable markets can be effectively competitive even where static market shares and static measures of concentration

[18] *See, e.g., Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corp. to WorldCom, Inc.*, Memorandum Opinion and Order, 13 FCC Rcd 180225, 18081 ¶ 101 (Sept. 1998) (*"MCI-Worldcom Merger Order"*).

might be high. The Commission has properly rejected claims that even a high market share permits the exercise of market power when any attempt to raise prices would be defeated by new sources of supply. In *AT&T Non-Dominance Order*,[19] for example, the Commission rejected claims that AT&T could exercise market power in the domestic long distance market at a time when AT&T served significantly more than half of all long distance customers. Despite AT&T's high static market share, the Commission concluded that it lacked market power because other long distance providers could and would "expand to serve additional AT&T customers should AT&T attempt to charge a supra-competitive price."[20]

51. The net effect of low concentration and easy entry is vigorous competition in all three of the regional markets the Commission has identified in the past: the "Atlantic, Pacific and Caribbean/Latin America" regions.[21] All three regions are served by multiple submarine cables, linked to end users by vigorously competitive transport markets. As the Commission recognized in 1998 when approving the merger of MCI and WorldCom, each of these three regions is served by numerous providers, "additional capacity will be provided by a growing number of suppliers," and barriers to entry were low.[22]

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[19] 11 FCC Rcd 3271 (1995).

[20] *See id.* ¶ 62.

[21] *See FCC Circuit Status Report*, Table 7; *MCI-WorldCom Merger Order* ¶ 94.

[22] *Id.* ¶¶ 86-114.

C. The Proponents Of Entry Regulation Have Failed To Show That Consortium Cables Facilitate Price Coordination

52. Neither the NPRM nor the pleadings of Global Crossing in the Japan-U.S. cable case have provided any plausible showing that consortium cable agreements promote or facilitate anticompetitive collective action by consortium members. Members market and price their services independently. McInerney Decl. ¶ 42. Furthermore, cable consortia do not impose any additional charges on individual owners for the volume of traffic handled. *Id.* Cable consortia thus are unlike rate bureaus, ocean shipping conferences, or agricultural cooperatives, in which multiple firms submit the pricing of their products and services to collective decision-making.

53. In addition, differences in the positions of different consortium members would make collusion difficult to implement because they lead to sharp conflicts of interest over the preferred collusive outcome. Some members have no capacity other than that in the consortium cable; others have large amounts of other capacity in the relevant market. Some are vertically integrated back into interexchange and global business markets at home; others are not. Moreover, these differences would create differential incentives and ability to "cheat" on any attempted implicit agreements to elevate prices and restrict output, thereby hampering enforcement of any such agreements and making them unlikely in the first place.

54. In any event, the antitrust laws should provide an adequate remedy for any collusion in pricing of services performed by participants in a consortium cable. Firms that market transport services on submarine cables that terminate in the United States are subject to its antitrust jurisdiction. Agreements to coordinate the prices of independently owned capacity

on consortium cables, whether made through the consortium structure or outside it, would clearly raise serious issues under the statutes that proscribe price fixing.

D. The Proponents Of Entry Regulation Have Not Shown That Consortium Cables Facilitate Anticompetitive Capacity Restrictions

55. The claim that submarine cable consortia facilitate anticompetitive restrictions on the capacity of new cables, and the expansion of capacity on existing cables, is equally unsupported. We understand that current FCC policy requires that promoters of a proposed cable project allow participation by all interested carriers, and that virtually all carriers with a conceivable interest in a consortium project are customarily invited to become equity owners. McInerney Decl. ¶ 42. Any carrier can acquire an interest in a cable by committing a proportionate share of the funds needed to build it. *Id.* The total initial capacity of a proposed consortium cable is limited only by the willingness of individual consortium members to pay for it. Moreover, consortium members are free to build or acquire capacity in competing lines. *Id.*

56. Once a cable is installed, consortium members will have to make decisions regarding capacity expansions. Such decisions are potentially quite complex, requiring careful attention to the aggregate supply and demand conditions in the relevant product and geographic markets, as well as meeting the needs of individual consortium members. For these reasons, some consortium cables require majority or supermajority approval for expansion of the capacity of a cable by means of upgraded electronics. Such governance provisions can serve as legitimate safeguards against potential free rider problems.[23] Because the incremental cost of capacity

[23] In fact, a private owner of a cable may also include a similar provision in its operational guidelines. This is because the private owner may have an incentive to offer incremental capacity to a new buyer at a low cost leading to a potential diminution in the value of the capacity leases

expansion is low (for any given level of initial capacity), individual carriers may have a strong incentive to invest in only a token amount of capacity on the original cable and then request expansion of cable capacity to meet their needs at the low incremental cost.

57. Carriers that engaged in this strategy would have lower costs—and thus could charge lower prices—than firms that shouldered the burden of contributing the funding that enabled the project to go forward in the first place.[24] Failure to prevent this kind of opportunism could lead to a race to the bottom, in which *no* carrier would be willing to be a sizeable investor in the initial cable capacity.[25] The obvious risk would be systematic underinvestment in cable projects, or even an inability to finance and build consortium cables at all. In any case, as this discussion makes clear, capacity expansions on the existing cable are complex business decisions that may require, for efficient disposition, responsive governance provisions and rules of pricing incremental capacity to consortium members as well as newcomers.

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to the initial purchasers. Realizing this incentive, the initial subscribers may insist on some provisions that would protect them from opportunistic *ex post* capacity expansions by the cable owner.

[24] Those carriers who bought initial capacity sufficient for their needs would likely not want to participate in the upgrade. Even if the added capacity could be bought at a price reflecting low incremental costs, these carriers may have no use for the additional capacity and thus would be reluctant to finance the upgrade, even if they obtained their *pro rata* share of the increment. On the other hand, it may be inefficient to cap the amount of added capacity going to the requesting carrier in accordance with the carrier's initial commitment. This is because the carrier may experience idiosyncratic growth in demand for its services that exceeds that of the other carriers.

[25] Indeed, if a private carrier cannot commit itself to not to engage in "opportunistic" capacity expansions on behalf of some carrier (or carriers), it may find itself without any buyers to begin with.

58. Any attempt to use the consortium structure and its governance rules to facilitate coordination of prices, output, and capacity growth would likely be self-defeating. First, as we have noted, the relevant geographic submarine cable markets are already competitive. Second, the absence of significant entry barriers enables those carriers who want additional capacity to build their own cable, or to obtain capacity on rival extant or forthcoming cables.

E. Global Crossing's Predatory Investment Scenario Is Also Unsupported

59. During the Japan-United States cable proceeding, Global Crossing advanced another theory of horizontal anticompetitive behavior that focuses on excessive investment in capacity: a theory which is inconsistent with Global Crossing's other claim that consortia cables underinvest in capacity. Under Global Crossing's scenario, a submarine cable consortium strategically deters competitive entry by building an *excessive* amount of spare capacity. Then, the consortium can credibly threaten to dump this excess capacity on the market and cause prices to fall substantially, should another competitor enter the market.[26] As a result, if a new cable operator were to enter, it would be unable to recover its upfront, sunk costs. Because the entrant anticipates this outcome, it chooses not to come in after all. In sum, in this scenario, excess capacity can deter efficient entry, even when the incumbent firm charges supra-competitive prices for its capacity.

60. The purported relevance of this scenario suffers from several obvious flaws. First, Global Crossing has offered no evidence that any consortium cable has actually pursued

[26] Actually, Global Crossing's theory of entry deterrence assumes that such a response is *ex post* profit maximizing. It need not be.

such a strategy. In fact, this scenario is flatly inconsistent with Global Crossing's repeated claims that cable consortia have systematically *undersized* their cables. *See, e.g., AT&T et al. Joint Application for License to Land and Operate a Submarine Cable Network Between the United States and Japan*, Response of Global Crossing to Supplemental Comments of Japan-US Cable Network *et al.*, File No. SCL-LIC-19981117-00025 at 41 (filed March 15, 1998).

61. Second, Global Crossing has not shown that the purported entry deterrence strategy is more profitable to the owner-investors of consortium cables, who have acquired interests in it for their own international traffic, than the efficient strategy of avoiding the costs of building significant excess capacity.

62. Third, Global Crossing's argument completely ignores the ability of potential entrants to safeguard against retaliatory price cuts by obtaining financial or volume commitments from the potential users of the new cable's capacity *before* making the sunk investments needed to build the facility. *See* McInerney Decl. ¶¶ 12-13. Making such commitments would be attractive to potential users of the new cable's capacity in the scenario contemplated by Global Crossing's argument, because under this scenario the incumbent cable owners are attempting to exploit market power by overcharging its customers. Once a new entrant has obtained these commitments and built its line, it cannot be dislodged by aggressive pricing by the incumbent cable operator.

63. Finally, if deterrence of competitive entry by overbuilding capacity were a problem, entry regulation by the Commission would not solve it. As noted above, cable capacity can be greatly and cheaply increased by upgrading the electronics at each end of the cable. *See*

McInerney Decl. ¶ 9. Entry regulation by the Commission does not govern or limit such expansion.

F. The Litigation Postures Of The Opponents And Supporters Of Proposed Consortium Cables Are Further Evidence That Entry By Cable Consortia Is Pro-Competitive, Not Anticompetitive.

64. The litigation postures of Global Crossing provides further confirmation that consortium cables tend to promote, not reduce, competition. If collusive or coordinated behavior had the effect of reducing the supply or increasing the price of capacity on consortium cables, Global Crossing, the supplier of a competing source of capacity, would benefit. Global Crossing's vigorous efforts to place roadblocks in the path of new consortium capacity warrants an inference that regulatory constraints sought by Global Crossing would lessen competition, not increase it.[27]

65. Conversely, many of the small carriers that Global Crossing seeks to attract have said that they prefer consortium cables, in part because consortium cables offer capacity that is considerably less expensive than the prices charged by closed investment cables. McInerney Decl. ¶ 40.

V. ENTRY BY CONSORTIUM CABLES GENERALLY DOES NOT RAISE VERTICAL FORECLOSURE CONCERNS

66. In arguing against entry by the Japan-US cable, Global Crossing also advanced two related scenarios of vertical foreclosure. In both scenarios, foreign monopolists use their

[27] Below, in section V, we show that the vertical foreclosure arguments, which possibly might justify Global Crossing's concerns, are not supported by empirical evidence.

supposed control over "essential" inputs to impede competition in the submarine cable market by discriminating among the participants in that market.

67. The first scenario entails a dominant foreign carrier strategically "clustering" carriers on a cable for which it operates landing stations. Here, the alleged rationale for this strategy is that the dominant carrier can gain additional profits by directing traffic to its landing stations, which are assumed to charge supracompetitive rates for the provision of landing services. Clustering is achieved (so the theory goes) not by denying rival cables access to landing stations, but by refusing to enter into "correspondent relationships" with carriers that utilize these rival cables. Global Crossing asserts that, unless a carrier can reach an operating agreement with the foreign country's dominant carrier, it cannot compete in the provision of international telecommunications services. This is because a carrier needs to receive profitable return traffic from the dominant foreign carrier so as to reduce its effective termination costs. *See* Joskow Decl. ¶ 42 (arguing that with "operating agreements, carriers are guaranteed return traffic in proportion to outbound traffic. Because settlement rates are above cost, having return traffic effectively reduces the cost of providing outbound minutes by offsetting some or all of the settlement for outbound termination. . . . If such inbound traffic is diverted away from a carrier disproportionately, that carrier's net marginal cost of termination is likely to increase . . . .").[28]

[28] Historically, IMTS traffic was moved across international boundaries pursuant to "correspondent relationships." The U.S. carrier would have an ownership interest up to the midpoint of the cable, whereas the foreign carrier would own the other half. The carriers would thus theoretically "hand-off" traffic to each other at this point. The rates carriers charged each other for terminating the traffic were determined by the international settlement rates. These settlement rates were historically significantly above cost. The terms of the correspondent relationship were embodied in a contract called an "operating agreement." Report and Order, *International Settlement Rates*, 12 FCC Rcd. 19806 (1997) (explaining that settlement rate benchmarks are required because "the rates U.S. carriers pay foreign carriers to terminate U.S.-

68. In the second scenario, a dominant foreign carrier discriminates against private cables in favor of consortium cables in which it has an ownership share. This theory requires that a dominant foreign carrier controls the backhaul facilities "necessary" for termination of traffic coming off a submarine cable. Thus, Global Crossing predicts that a dominant foreign carrier will deny access to its backhaul to submarine cables that compete with the cable(s) in which it has ownership interests.[29] Allegedly, by shifting away traffic from the rival cable and onto its cable, the dominant firm will be able to elevate its profits and harm consumers. GC Reply at 15-16.

69. Neither of these two scenarios raises concerns that are realistic in the actual markets for the services of submarine cables today and going forward. We discuss each in turn.

A. Clustering

70. The clustering scenario fails for several important reasons. First, operating agreements are not essential inputs. The Commission has found that "[g]enerally, U.S. carriers are able to obtain operating agreements or establish alternative arrangements to provide international services."[30]

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originated traffic are in most cases substantially above costs foreign carriers incur to terminate that traffic.").

[29] Presumably, this anticompetitive scenario requires only that the dominant firm offers backhaul on discriminatory terms to rival cables.

[30] MCI-WorldCom Merger Order ¶ 117. *See also AT&T International Non-dominance Order* ¶¶ 50-51.

71. Second, Commission regulatory policies and increasing competition in foreign markets have been forcing settlement rates down toward termination costs. As increasing numbers of countries adopt benchmark settlement rates, many countries have reduced rates to even lower levels, and more U.S. inbound traffic is terminated at cost-based rates. *See* AT&T Comments Part II.C.1. These trends generally diminish the importance of return traffic – the central predicate of the clustering theory – to carriers providing outbound services from the United States.

72. Third, traditional correspondent relationships are only used for IMTS traffic terminated on the public switched network. Internet, voice and data traffic carried on private line circuits are exempt from the settlement process and does not earn proportionate return. Hence, carriers could circumvent and defeat the anticompetitive strategy hypothesized by Global Crossing by carrying data traffic or shifting switched voice traffic to private lines. We understand that less than 5 percent of current traffic is IMTS and that cable planners generally do not even take this traffic into account when planning cable system.[31] Commission statistics show that over 80 percent of new active international submarine cable circuits from 1995-98 were private line circuits, rather than IMTS circuits.[32] Industry experts estimate that data traffic will become 25 times greater than voice over the next five years, accelerating this trend still further.[33]

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[31] *See* McInerney Decl. ¶ 10.

[32] *FCC Circuit Status Report*, Table 2.

[33] *See* The Economist, Mar. 13, 1999 at 82; Wall Street Journal Europe, Convergence magazine Mar. 15, 1999.

73. Thus, even if every incumbent foreign firm announced that it would enter into correspondent relationships only with those carriers that used the submarine cables affiliated with the foreign firm, the vast majority of the telecommunications market would remain open to carriers that use different cables. Hence, the clustering strategy hypothesized by Global Crossing would create incentives to shift traffic onto private lines operated by competitors of the foreign firms (including, in an increasing number of countries, U.S. firms that have been authorized to enter the foreign market), thereby denying the dominant firm whatever revenues it may have earned on the diverted traffic. The effect is, of course, that the contemplated strategy is likely to be unprofitable.

74. Finally, the clustering argument implicitly assumes that the relevant market for submarine cable is point-to-point country pairs. As noted above and documented in the Declaration of Mr. McInerney, however, submarine cables tend to serve broad geographic regions. Carriers can shift traffic between landing stations in a particular region – even when they are in different countries – in order to lower the overall costs of terminating a call. Also, carriers can route traffic via terrestrial facilities at the *originating* end among the various cables in which they have an interest to avoid a particular landing station that is charging excessive rates. Such substitution among landing stations is made possible by the fact that most cables land in multiple countries within a single region. If carriers on a cable that lands in countries A and B could use a landing station in A to route traffic to B (or vice versa), then neither landing station owner would be able to charge supra competitive rates. The carrier would simply shift traffic to the owner offering competitive rates. Put another way, competition among landing stations offers a constraint on the ability of any landing station owner to exercise market power, thereby

making it unlikely that the "clustering" strategy of vertical leverage will be profitable in the actual submarine cable markets.

B. Denial Of Access To Backhaul Facilities

75. Global Crossing's alternative scenario—vertical foreclosure of unaffiliated submarine cables through denial of access to backhaul facilities—is equally unfounded in the economic realities of international telecommunications markets. First, for such a strategy to work, the foreign carrier must possess a backhaul monopoly. If competition exists in the foreign-end backhaul market, no carrier can impede entry by submarine cables. If a carrier refuses to provide backhaul service to carriers using a particular submarine cable (or provides poor service), these carriers can simply turn to alternative backhaul providers. For example, we understand that Global Crossing, while claiming that the Japanese market is monopolized by NTT/KDD, was nevertheless able to arrange for termination of its traffic by competitive carriers.

76. But where such a backhaul monopoly truly exists, Global Crossing's second foreclosure theory is largely irrelevant. It would be pointless to deny U.S. landing licenses to consortium cables serving countries that lack backhaul competition and competitive cable landing arrangements. Where only the monopoly carrier may lawfully operate facilities in the foreign country for traffic origination and termination, U.S. carriers cannot make independent arrangements for collocation and self-provision of backhaul at foreign cable stations. All U.S. carrier arrangements must be with the foreign monopoly carrier, with all traffic handed-off to the foreign monopoly carrier mid-ocean and terminated at the foreign end subject to settlement rates negotiated with that monopoly carrier.

77. Second, the carrier that controls the foreign backhaul facilities would be unlikely to have incentives to undertake this foreclosure strategy, unless it owns a significant percentage interest in the affiliated submarine cable. This is because discriminating against the traffic of an unaffiliated submarine cable would likely lower overall demand for its backhaul services. For example, this would be the consequence of some product or brand differentiation among carriers operating on the disadvantaged cable and those operating on the advantaged cable. Consequently, not all of the traffic diverted from the disadvantaged cable would be recouped by the advantaged consortium partners. Then, unless the foreign carrier has significant ownership interest in a cable, it is more likely to lose revenues than gain revenues from a "foreclosure" strategy. A foreign carrier with only a small ownership interest in its affiliated consortium cable would likely lose more from the overall reduction in traffic than it could capture from stimulation of its own demand. We are unaware of any recent or planned consortium submarine cable landing in the U.S. in which a dominant foreign carrier has more than a 25% ownership interest. For example, NTT's interest in Japan-US cable is only about 4 percent. *See* McInerney Decl. ¶ 2.

VI. REGULATORY OVERSIGHT OF NEW ENTRY SHOULD BE LIMITED TO REFLECT THE COMPETITIVE STRUCTURE OF THE SUBMARINE CABLE INDUSTRY

78. As explained above, the structure and the dynamic nature of the submarine cable industry warrants a strong presumption that entry, whether by consortium cables or by private cables, is pro-competitive and in the public interest. Neither the NPRM nor the proponents of entry regulation have advanced any argument that successfully rebuts this presumption. Because

Commission regulation of entry is costly and likely to impede competition, the Commission should presumptively streamline all submarine cable landing license applications.

79. We understand that the Commission approves most international Section 214 applications under a "streamlined procedure in which public comment will not be sought, and petitions to deny will not be entertained, on competitive and other issues."[34] This is even true of applications by carriers in which *dominant* foreign carriers have substantial ownership interests. The Commission found that no significant competitive issues were raised by a dominant foreign carrier owning up to a 25% interest in a domestic carrier, because that level of ownership was insufficient to give the foreign carrier "incentive to discriminate in favor of the affiliated carrier."[35]

80. There is no reason, and the NPRM does not offer one, why the streamlined procedures for cable should not follow the procedures adopted in the *International Section 214 Order*." As such, all applications that qualify for streamlining should be approved in 14 days upon public notice.[36] Approval should be withheld past the end of the 14 day time period only for applications that are incomplete, that do not qualify for streamlining (if the Commission were to adopt a more "targeted" approach), or those few applications that Commission Staff identify

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[34] *International Section 214 Order* ¶ 22.

[35] *Id.* ¶ 32.

[36] The NPRM proposes a 60-day period because of the need to "coordinate closely with the Executive Branch." NPRM ¶ 54. But, we understand that the Commission can grant an application subject to ultimate approval by the Secretary of State and continue to work with the Secretary of State with regard to her approval. In this way, greater certainty can be created sooner for the applicant, helping to dissipate unnecessary regulatory risk.

as "rais[ing] extraordinary issues suggesting a need for public comment."[37] Further, "public comment [should] not be sought, and petitions to deny [should] not be entertained, on competitive and other issues."[38] The likelihood that a qualifying application would impair competition is "so remote that the potential benefits of seeking such comment are outweighed by the real benefits of eliminating the possibility that such comments would render an application ineligible for streamlining."[39]

81. These key elements of the Commission's analysis underlying the International Section 214 Order certainly do apply here, as we have shown. Unless the window for challenging submarine cable landing applications is short, and the criteria appropriately narrow, regulatory delay would continue to be an unnecessary and significant potential barrier to entry.

82. To refute the presumption that entry is competitively beneficial or harmless, opponents of a proposed transaction should be required to demonstrate, consistent with the standards and principles of the Competitor Collaboration Guidelines, that the proposed entry creates a significant likelihood of injury to competition, and not merely harm to competitors.[40]

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[37] *International Section 214 Order* ¶ 16.

[38] *International Section 214 Order* ¶ 22.

[39] *Id.* ¶ 12. Among the substantial "real benefits" identified by the Commission in the international Section 214 context is "the added certainty that an applicant would have as a result of knowing its application cannot be held up by a vaguely drafted petition to deny filed by its competitors." *Id.*

[40] We do not necessarily embrace all the elements of the analytical approach to the assessment of competitive effects of competitor collaborations, as developed in the Guidelines. However, since in our view the Guidelines offer a stringent set of hurdles which a collaboration must pass before it is deemed not anticompetitive, requiring that the opponents meet the Guidelines test will likely not lead to anticompetitive entry being allowed. If anything, the danger is that some pro-competitive entry may be deterred.

The burden should be on the party challenging the entry to explain precisely how the harm to competition is likely to occur, and to identify the specific circumstances that warrant an exception to the general presumption that the entry of additional submarine capacity is procompetitive and inures to the benefit of telecommunications consumers.

VII. THE THREE STREAMLINING OPTIONS PROPOSED IN THE NPRM ARE INCONSISTENT WITH THE COMPETITIVE STRUCTURE OF THE SUBMARINE CABLE INDUSTRY

83. The regulatory regime proposed in the NPRM is fundamentally at odds with the economic principles discussed above. Rather than start with the presumption that new entry is pro-competitive, the NPRM instead would permit streamlining in only a few, narrowly defined, circumstances. This approach would impose regulatory costs on many proposals for competitive and beneficial entry, would delay such beneficial entry, and would pressure applicants to structure their transactions in ways that are potentially inefficient and, possibly, harmful to the public interest.

A. The Competitive Route Option (NPRM ¶¶ 25-32)

84. This option is plainly inconsistent with sound public policy. Under this option, there would be expedited (streamlined) assessment of new cable projects on routes that are sufficiently served by submarine cables to be competitive, but not of cable projects on routes where there is little competition and that would benefit the most from new entry. NPRM ¶ 25. We agree with the Commission that where competition reigns, no regulatory scrutiny is necessary. However, we also insist that only streamlined assessment, at most, is necessary on routes that have limited submarine cable offerings. As explained above, market forces, not

regulators, should generally dictate where entry should occur. Instead of trying to micro-manage entry decisions, the Commission should adopt policies that reduce entry barriers and encourage investment so that cables can be built to serve any location where investors believe that demand has already, or likely will, outpace supply.

1. Regional markets for assessing competitive routes

85. If the Commission were to decide to retain the Competitive Route Option, it should use regional markets to assess whether the route is "competitive." Basing the analysis on markets that are arbitrarily confined to point-to-point routes is plainly not consistent with competitive realities in international telecommunications markets and may disqualify from streamlined treatment proposed cables on routs that are, in reality, highly competitive. As noted above, international transport markets are highly competitive, and U.S. carriers now provide services to many countries via carriers in third countries by deploying switched hubbing, refile, reorigination and transit services.

2. The number of independent cable entrants

86. Under the NPRM, the Commission will deem a route competitive and thus ripe for streamlined procedures if three "independent" cables became operational on the route within the previous 36 months. We agree with the Commission that evidence of past entry is indicative of a lack of significant impediments to entry. We also agree that a regional market populated by three modern cables is likely effectively competitive. However, we conclude that this criterion is too strenuous in several respects. First, as explained above, the effectiveness of competition on a regional route is not a function solely of the number of cables on a particular route. Because the

fractional ownership interests on consortium cables are independently priced and marketed, effective competition can in principle exist among the participants in a single consortium cable.

87. Second, the relevant product market should also include transport by telecommunications satellites. Satellite systems are increasingly being used for data transmission, which has a significant and rapidly growing share of international telecommunications traffic. As such, satellite transport constrains the rates that cable operators can charge for data transmission. Because voice and data are not generally subject to different pricing, these forces of competition from satellite transport also operate on and constrain cable voice transmission charges.

88. Third, because barriers to entry are low, effective competition can coexist with high market shares and levels of concentration. *See* ¶¶ 44-54, above. Moreover, even if fewer than three entrants came in over the relevant 36-month period, this is no indication that the relevant market is not effectively competitive. For example, a market may not be able to support three new cables, given the existing supply and demand balance.

89. Fourth, it is economically and factually arbitrary for the NPRM to consider only those cables that have become operational in the last 36 months. The NPRM asserts that it adopted this time period because "cables built with older technologies may not support significant capacity expansion."[41] As explained in the accompanying Declaration of Mr.

[41] NPRM ¶ 28.

McInerney, there are numerous submarine cables that have been operational for more than three years and that use fiber optic technology that permits significant capacity expansion.[42]

3. Attribution

90. The NPRM seeks comment on how the Commission can determine whether a cable is "independent" in the context of its standard that "three recent independent cable entrants implies competition." As explained above, a proper competitive analysis focuses on the amount of capacity controlled by an independent entity in a region, and whether alternative sources of supply are insufficient to prevent that entity from profitably raising prices. As noted above, no carrier today controls sufficient capacity in any of the three regions to exercise such market power. Indeed, barriers to entry into submarine cable markets are sufficiently low that even an entity that controlled a substantial share of capacity in a particular region could not profitably raise prices for more than a very brief period. Such an attempt would prompt other providers to enter the market, or existing competitors to expand capacity. The resulting loss of customers would make the price increase unprofitable.

91. The NPRM also seems to adopt the premise that if an entity controls the only landing station in a particular country, it effectively controls the cable.[43] This presumption ignores the reality of contractual relations between the entity controlling the landing station and the members of a consortium of owners of the cable employing it. As explained above, the various members of a consortium cable have the ability and impetus to protect themselves from

[42] *See* McInerney Decl. ¶¶ 30-38.

[43] *See* NPRM ¶ 30.

undue control by the owner of the landing station *ex ante* through contractual arrangements. A particular landing station is used only when the project sponsors agree on that selection. Clearly, the cable owners (other than an owner that would control the landing station) have no desire to pay excessive rates for landing services, and no desire to cede control of their marketing decisions to the landing station management. These owners will use their *ex ante* negotiating leverage to establish a contract that keeps this from happening.

92. More importantly, most modern submarine cables are served by multiple landing stations. The NPRM recognizes that where carriers on a particular cable have at least two independently owned and operated landing stations to choose from, it is unlikely that either station will be able to charge excessive rates.[44] However, the NPRM incorrectly limits this safe harbor to those situations where the available landing stations are in the same country.[45] As explained above, the relevant market is *regional*, not country-specific. Thus, even an entity that controls the only landing station in a particular country, it will be constrained in its rates if the carriers can switch traffic to other landing stations in that region. Thus, for example, although TAT-14 is served only by one landing station in France, that operator could not profitably charge supracompetitive rates. If it tried to do so, the carriers using TAT-14 would respond by shifting traffic to stations in Britain, Denmark, Germany, and the Netherlands, and then using alternative transit arrangements to route the traffic into France. *See* McInerney Decl. ¶¶ 21-29.

[44] NPRM ¶ 30.

[45] *Id.*

93. Finally, even if a submarine cable were served by only a single landing station in a region, there should be no attribution where the landing station operators have agreed to permit the cable owners to collocate at that landing station. Such competitive collocation effectively constrains the ability of landing station operators to charge excessive prices to the competing cable systems because the competing cable systems could simply collocate their own equipment in the landing station and by-pass the landing station bottleneck. *Japan-US Cable Order* ¶¶ 28-29.

B. The Competitive Capacity Expansion Option (NPRM ¶¶ 33-37)

94. This proposal would discriminate arbitrarily in favor of "new entrants" and against many existing carriers without any economic justification. The NPRM appears to suggest that streamlined treatment under this option will be denied where the members of the "key applicant group" collectively own more than half of existing wet link capacity. NPRM ¶ 33-34. Although the NPRM does not state so explicitly, presumably this threshold will be met by summing the individual ownership interests of all the members of the key applicant group. For example, if there were three key applicants for a proposed cable, streamlining would be denied if the three key applicants had individual interests in existing cable systems in that region that, in aggregate, exceeded 50 percent of existing capacity.[46]

95. This rule makes no sense, however, unless there is an unstated presumption that the members of the key applicant group act as a single entity rather than as competitors in their

[46] Paradoxically, the NPRM also suggests that the Commission is considering withholding streamlining when *all* the participants in a project are new entrants.

use of their capacity. Typically, however, the members of the key applicant group are (or will be) independent competitors who make independent pricing and marketing decisions over the uses of the capacity shares that each one owns. Then there is no economic significance to the total ownership interest in cable capacity held by the key applicant group members, and streamlining should not be denied to the application on this basis.

96. The economic shortcoming of the prerequisites for availability of this streamlining option is even plainer when the "key applicant group" does not also control each of the existing cables in the same proportion as it controls the proposed consortium cable. This can be shown with a simple hypothetical. Suppose that X, Y and Z comprised the "key applicant group" for a new cable, and in that region there were three existing cables. Further, assume that X, Y and Z each individually owns 100% of one of the three cables.[47] While collectively, X, Y and Z would own 100% of the existing cable capacity, individually each would have one-third of existing capacity and they would all compete against one another. Accordingly, X, Y and Z as a group would have no interest in taking actions that favored any particular privately owned cable. Thus, for example, while X might have incentive to have the new cable take actions that would favor its existing cable (assuming such actions were even possible), Y and Z would not.[48]

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[47] Assuming that the cables have the same capacity.

[48] Nor can it be argued that the application is problematic because somehow the new cable would give A, B and C additional incentive to collude. The additional capacity available to each party would enable each to profit more by selling more in competition with the others. Colluders want to limit the amount of available capacity, not increase it. In other words, if A, B and C wanted to restrict capacity they would not seek to build a new cable but instead would jointly agree to refrain from such projects.

97. Similarly flawed is the NPRM's conclusion that it will attribute the entire capacity of an existing cable to any entity that owns 50% or more of the equity of an existing cable. NPRM ¶ 35. Merely owning 50% of a cable does not necessarily enable an entity to dictate the pricing and marketing decisions of the minority owners.

98. Further, the proposed approach could lead to plainly inaccurate and distortionary results. Suppose, for example, that a market is served by four cables that A owns 51% of the two of them, that B owns 100% of the remaining two, and that B also owns 49% of the two cables in which A is the majority owner. Under this rule, A would be considered to control 50% of the wet link capacity in this market – and be disqualified from the "competitive capacity expansion" streamlining option – even though it (hypothetically) owns only approximately 25% of total cable capacity,[49] likely will have no ability to exercise market power, and its entry likely will stimulate output in and competition in the relevant market.

99. Finally, the NPRM's proposed methodology for attributing wet link ownership based on ownership of cable landing stations should also be rejected as not being grounded in economics or current market realities. The NPRM proposes to attribute wet link ownership in direct proportion to cable landing station ownership in a particular country. NPRM ¶ 33, 35. Because many modern submarine cables land in multiple countries, this attribution rule could assign landing station owners more than 100 percent of the actual capacity. The TAT-15 cable, for example, has landing stations in five different European countries. It is the individual owners of the cable capacity that can compete with one another over the sales of services that utilize that

[49] Assuming again that all the cables have equal capacity.

capacity, and the owners of different landing stations may well be competitors of one another in the same relevant regional geographic market. Then, in no sense are the levels of competitive significance of the owners of the cable capacity indicated by the shares of cable landing station ownership in a particular country.

C. Pro-Competitive Arrangements Option (NPRM ¶¶ 38-50)

100. This option seems to be designed to stimulate or to induce operators to adopt, as inducement for trade streamlining, an array of policies that, according to the NPRM, would increase competition. Since the NPRM does not dispute that the relevant markets are already competitive today,[50] it appears that this option constitutes an attempt to utilize the carrot of avoidance of unnecessary regulatory delay and risk to encourage adoption of business decisions that would meet with Staff's approval. Such a policy approach should be eschewed since the relevant markets are generally competitive, and regulatory delays and risks are costly. Independent competitive business decision-making should be given precedence over regulatory attempts to micro-manage entry. Moreover, it is not at all clear that the arrangements that this option seeks to promote are more likely to facilitate competition than to impede it.

101. To qualify for the "pro-competitive arrangements" option, for example, owners would have to upgrade capacity, not on the basis of arm's length negotiations, but according to

[50] The NPRM offers the offhand suggestion that the so-called "pro-competitive arrangements" might be appropriate because they could help to "constrain the incentive of landing parties to induce small carriers to join on their cable, to the exclusion of competitors' cables . . ." *Id.* ¶ 39. This appears to be a reformulation of Global Crossing's "clustering" arguments. The clustering theory is untenable for the reasons explained at ¶¶ 70-74, above.